IGM
Initiative on Global Markets
2020–21

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A Year Like No Other

The 2020–21 year proffered new challenges and interesting opportunities for the Initiative on Global Markets (IGM). Recognizing that much of our event lineup did not translate into a virtual environment, the IGM opted to explore a new avenue: survey collaborations. The first of these partnerships, the FiveThirtyEight/IGM COVID-19 Economic Outlook Survey, commenced in May of 2020 and continued until just before the presidential election of November 2020. The newest collaboration, the FT-IGM US Macroeconomists Survey, launched in June 2021. In line with our mission, these items represent exciting growth and diversification, and are new facets that position the IGM well for the future.

Our Mission

The Initiative on Global Markets aims to organize Booth faculty efforts to “influence public policy and the practice of business” around the world. As such, it focuses on three broad forms of engagement. They are:

Expert Panels—Through its unique experts panels, the IGM helps inform the public, policymakers, and journalists of how top US and European economists think about important questions of the day.

Visitors—The IGM sponsors campus visits of policymakers, public intellectuals, business leaders, and journalists to create opportunities for interactions with Booth faculty and the broader university community.

Conferences—The IGM sponsors the USMPF, an annual high-visibility conference on a monetary policy issue in the United States, as well as other large-scale conferences on different, timely public policy topics. It also organizes smaller, private meetings between policymakers, academics, and business leaders that foster frank discussions on topics of mutual interest and encourages an exchange of thoughts, ideas, and knowledge.

Collectively, these activities raise the impact of Chicago Booth research, catalyze new research ideas, and more generally enrich the Chicago Booth environment.
Thank You
The IGM is grateful for the generous support provided by our many supporters, especially Leslie Barbi, ’93, and Aaron S. Bell; Thomas Batten, ’12; Ramsey A. Frank, ’86; and Constance M. Frydenlund, ’87, and John Covell.

New and Notable
The FT-IGM US Macroeconomists Survey launched in June 2021. Professors Allan Timmerman (UC San Diego) and Jonathan Wright (Johns Hopkins University) with Colby Smith (Financial Times) develop the surveys that are then posed to a standing group of 57 well-known macroeconomists. The resulting articles are posted on the Financial Times site under the tag, FT-IGM US Macroeconomists Survey, while the summary data from each round is posted on the IGM Forum (igmchicago.org/ft-igm-us-macroeconomists-survey). Although in its infancy, the collaboration is already very promising, and we look forward to a bright future for this partnership.
This collaboration between FiveThirtyEight and the IGM started in May 2020 and continued until late October 2020. In it, leading economic forecasters provided a nuanced understanding of the economic challenges facing the United States as a result of the COVID-19 pandemic. To gauge developments over time, certain questions were posed each round alongside new timely questions. Thus, as the months passed, the surveys reflected on not only the rapidly changing economic environment, but current developments in the course of the pandemic. The success of this short-term association set the groundwork for future endeavors along the same lines.

The articles stemming from these surveys can be found on FiveThirtyEight site via the links to the right and the summary results for each of the 10 surveys is on the IGM Forum (igmchicago.org/economic-outlook-survey).
“Following the Global Financial Crisis of 2007–09, the US and other economies shored up the resilience of their banks through more demanding capital and liquidity requirements and rigorous stress testing. The disruptions of financial markets at the onset of the pandemic in March 2020 underscored the vulnerabilities of markets and institutions that comprise the important—and growing—nonbank sector of the financial system through which much credit to businesses, households, and government flows.

The Task Force on Financial Stability was formed before the pandemic, in October 2019, by the Hutchins Center on Fiscal and Monetary Policy at the Brookings Institution and the Initiative on Global Markets at the University of Chicago Booth School of Business. Its mission was to identify gaps in the regulatory architecture and other features of the financial system (outside the regulated banking sector) that make it insufficiently resilient, and to recommend mitigating policies to regulators, Congress, and the industry.

The report focuses on the US Treasury market, open-end mutual funds, housing finance, derivatives clearinghouses, and life insurance companies; it also makes recommendations for the structure and process of regulation, including the Financial Stability Oversight Council and the Office of Financial Research, both created by the Dodd-Frank Act, to increase the likelihood of spotting and addressing issues that will arise in the future.”

—Hutchins Center on Fiscal and Monetary Policy at the Brookings Institute

(Above quote taken from a Brookings press release)

Use this link to read the Task Force on Financial Stability report

Watch the report release on YouTube and download the accompanying slide deck.
The Economic Experts Panels are two groups—US and European—comprised of preeminent economists from a variety of specialties. Each panel of 40-plus scholars responds to polls on timely, relevant topics that reflect current economic issues and discussions from around the world.
Panelist Highlights

This year several new panelists joined the European Panel:

• Oriana Bandiera, London School of Economics
• Carol Propper, Imperial College, London
• Sergei Guriev, Sciences Po, Paris
• Imran Rasul, University College London
• Ricardo Reis, London School of Economics
• Kjetil Storesletten, University of Oslo
• In Memoriam: European Panelist, Peter Neary, passed away in June 2021.

News

Over the course of the 2020–21 year, the IGM initiated the first phase of a site-wide renovation of the IGM Forum (igmchicago.org). The first part of the overhaul went live in September 2020. It included a new look that provides a better interface—the first step towards becoming digitally accessible—and more functionality. Now, the site is not only mobile, and tablet-friendly, but includes new features such as survey data files, contextual information regarding specific surveys, and a more robust search feature that enables users to quickly and easily find specific surveys or articles.
Coordinators

Romesh Vaitilingam works in concert with Anil Kashyap (US Panel) and Christian Leuz (European Panel) to develop the questions for each poll.
US Poll Highlights

“It walks, swims, and quacks like a duck, it’s probably a duck. It looks, behaves, and dominates like a monopoly, it’ll probably harm welfare.”

“The recession is a public health emergency, and stimulus without first addressing the health issues can be ineffective or counterproductive.”
—Larry Samuelson, Yale, commenting on Coronavirus Relief: igmchicago.org/surveys/coronavirus-relief/

“With ten reliable vaccines available, the issue is not patent protection. It is manufacturing and distribution.”
—Pinelopi Goldberg, Yale, commenting on Vaccines for Developing Countries: igmchicago.org/surveys/vaccines-for-developing-countries/

Panelists’ Responses Regarding Question A: Reliable Covid-19 vaccines will reach developing countries more quickly if the rich countries pay the pharmaceutical companies at prevailing prices to manufacture and distribute the vaccines (or to license production and support licensees), rather than waiving patent protection.

Panelists’ Responses Regarding Question C: Extension of the suspension of payments on student loans after the end of the year would support the recovery more effectively than devoting equivalent resources to general income-based transfer payments.

Panelists’ Responses Regarding Question C: The nature of the market dominance of technology giants in the digital economy warrants either the imposition of some kind of regulation or a fundamental change in antitrust policy.

INITIATIVE ON GLOBAL MARKETS, 2020–21
Panelists’ Responses Regarding

Question B: The ECB should take account of the environmental implications of its policy decisions.

- 15% Strongly agree
- 37% Agree
- 11% Uncertain
- 31% Disagree
- 6% Strongly disagree

Panelists’ Responses Regarding

Question C: A public policy goal that could be accomplished with a well-enforced wealth tax could be accomplished at lower cost with modifications to existing taxes, such as income tax, capital gains tax, inheritance tax and property tax.

- 11% Strongly agree
- 50% Agree
- 29% Uncertain
- 10% Disagree
- 0% Strongly disagree

Panelists’ Responses Regarding

Question C: A global corporate tax system that is based on the location of final consumers would be more efficient than one based on the location of corporate headquarters and production facilities.

- 19% Strongly agree
- 32% Agree
- 47% Uncertain
- 2% Disagree
- 0% Strongly disagree

“All serious Brexit analysis shows a significant hit to the UK because of higher trade costs with its nearest neighbor.”
—John Van Reenen of the London School of Economics and MIT, commenting on After Brexit: igmchicago.org/surveys/after-brexit-2/

“A no-brainer. We need to save the planet; everyone should take into account the environmental implications of their decisions, even the mighty.”
—Christopher Pissarides, London School of Economics and Political Science, commenting on Objectives of the European Central Bank: igmchicago.org/surveys/objectives-of-the-european-central-bank/

“An obvious case of natural monopoly. Unfortunately, it is (almost) at the global level so countervailing action would have to be global too.”
Conferences take various forms, including discussion panels, political debates, and lectures by individuals. Featured speakers range from members of Chicago Booth’s faculty to global economic leaders.

Events
The Global Economy and Financial Stability Conference
July 2020, September 2020, and May 2021

The IGM hosted virtual conferences (in July and September 2020, and May 2021) to discuss the state of the global economy and issues related to financial stability. The conference consisted of an off-the-record discussion among central bank and government officials, senior financial services executives, and academic economists.

Coping with the Labor Market Consequences of the Pandemic
August 14, 2020

As Congress and the President discussed whether further assistance for the economy is warranted, the IGM convened a conversation amongst Steven J. Davis, Casey B. Mulligan, and Joseph S. Vavra, and moderated by Robert H. Topel. Our panelists discussed what we know about the short-run effects of the CARES Act measures, what they expected the medium-term effects of the act to be, and what types of policies would be good and bad for facilitating further adjustments in the labor market. Each panelist offered 10 minutes of opening comments, followed by a group conversation, and audience Q&A.
The Initiative on Global Markets is a resource for those who seek to critically analyze the day’s most pressing issues. To that end, we fund research projects in the areas of international business, financial markets, and public policy. Our goal is to foster an exchange of ideas and evidence in order to generate insights that can help solve the biggest issues facing people in the rapidly changing global economy.

The following are working papers from this year.
This paper presents a simple price-theory approach to COVID-19 lockdown and reopening policy. The key idea is to conceptualize $R \leq 1$ as a constraint, allowing traditional economic and societal goals to be the policy objective, all within a simple static optimization framework. This approach yields two main insights. First, the $R \leq 1$ constraint imposes a disease-transmission budget on society. Society should optimally spend this budget on the activities with the highest ratio of utility to disease-transmission risk, dropping activities with too low a ratio of utility to risk. Second, masks, tests, and other simple interventions increase activities' utility-to-risk ratios, and hence expand how much activity society can engage in, and utility society can achieve, while staying within the $R \leq 1$ budget. A simple numerical example, based on estimates from the medical literature for $R_0$ and the efficacy of face masks and complementary measures, suggests the potential gains are enormous. Overall, the formulation provides economics language for a policy middle ground between society-wide lockdown and ignore-the-virus approaches, and a new infectious threat response paradigm alongside “eradicate” and “minimize.”

This paper builds a new model of financial exchange competition tailored to the institutional details of the modern US stock market. In equilibrium, exchange trading fees are competitive but exchanges are able to earn economic profits from the sale of speed technology. We document stylized facts consistent with these results. We then use the model to analyze incentives for market design innovation. The novel tension between private and social innovation incentives is incumbents’ rents from speed technology in the status quo. This creates a disincentive to adopt new market designs that eliminate latency arbitrage and the high-frequency trading arms race.
Tracking human activity in real time and at fine spatial scale is particularly valuable during episodes such as the COVID-19 pandemic. In this paper, we (Dingel and coauthors Victor Couture, Allison Green, Jessie Handbury and Kevin R. Williams) discuss the suitability of smartphone data for quantifying movement and social contact. We show that these data cover broad sections of the US population and exhibit movement patterns similar to conventional survey data. We develop and make publicly available a location exposure index that summarizes county-to-county movements and a device exposure index that quantifies social contact within venues. We use these indices to document how pandemic-induced reductions in activity vary across people and places.
We (He and coauthors Jiangze Bian, Zhi Da, Dong Lou, Kelly Shue, and Hao Zhou) use granular data covering regulated (brokerage-financed) and unregulated (shadow-financed) margin trading during the 2015 market turmoil in China to provide the first systematic analysis of margin investors’ characteristics, leverage management policies, and liquidation choices. We show that leverage constraints induced substantial forced and preemptive sales, and leverage and cash management differed substantially across investor and account types. We explore the relation between margin trading and shock propagation, and show that China’s price limit rule led to unintended contagion across stocks. Compared to brokerage investors, shadow investors were closer to their leverage constraints, and played a more significant role in transmitting shocks across stocks.
We (Hornbeck and coauthor Martin Rotemberg) examine impacts of market integration on aggregate productivity growth in the United States, as railroads expanded in the 19th century. Using data from the Census of Manufactures, we estimate relative increases in county manufacturing productivity from relative increases in county market access. In general equilibrium, we find that the railroads substantially increased economic activity in marginally productive counties. By allowing for factor misallocation, we estimate much larger aggregate economic gains from the railroads than previous estimates. Our estimates highlight how broadly-used infrastructure or technologies can have much larger economic impacts when there are inefficiencies in the economy.
We (Kashyap and coauthors Natalia Kovrijnykh, Jian Li, and Anna Pavlova) argue that the pervasive practice of evaluating portfolio managers relative to a benchmark has real effects. Benchmarking generates additional, inelastic demand for assets inside the benchmark. This leads to a “benchmark inclusion subsidy”: a firm inside the benchmark values an investment project more than the one outside. The same wedge arises for valuing M&A, spinoffs, and IPOs. This overturns the proposition that an investment’s value is independent of the entity considering it. We describe the characteristics that determine the subsidy, quantify its size (which could be large), and identify empirical work supporting our model’s predictions.

I review the workings of the United Kingdom’s Financial Policy Committee to illustrate the challenges of implementing macroprudential policy. I describe the committee’s remit, explain my views on the channels of financial instability that the committee tries to mitigate, describe the tools the committee has at its disposal and outline the principles it uses in deploying these tools. I conclude by offering some of the lessons I have learned in serving on the committee and highlighting a few challenges for macroprudential policymakers.
We (Kashyap and coauthors Natalia Kovrijnykh, Jane Li, and Anna Pavlova) propose a model of asset management in which benchmarking arises endogenously, and analyze its unintended welfare consequences. Fund managers’ portfolios are unobservable and they incur private costs in running them. Conditioning managers’ compensation on a benchmark portfolio’s performance partially protects them from risk, and thus boosts their incentives to invest in risky assets. In general equilibrium, these compensation contracts create an externality through their effect on asset prices. Benchmarking inflates asset prices and gives rise to crowded trades, thereby reducing the effectiveness of incentive contracts for others. Contracts chosen by fund investors diverge from socially optimal ones. A social planner, recognizing the crowding, opts for less benchmarking and less incentive provision. We also show that asset management costs are lower with socially optimal contracts, and the planner’s benchmark-portfolio weights differ from the privately optimal ones.

We (Kashyap and coauthor Takeo Hoshi) take some well-known observations about the structure of the Japanese labor market and add new evidence about how it has evolved to study inflation in Japan. Our key finding is that labor market dynamics shifted after 1998 so that correlations between labor market tightness and wages weakened noticeably. This change was accompanied in a break in the relationship between wages and prices, so wage inflation has become a much less important determinant of price inflation.
Over the past 15 years, the typical household has increasingly concentrated its spending on a few preferred products. However, this is not driven by “superstar” products capturing larger market shares. Instead, households increasingly purchase different products from each other. As a result, aggregate spending concentration has decreased. We develop a model of heterogeneous household demand and use it to conclude that increasing product variety drives these divergent trends. When more products are available, households select products better matched to their tastes. This delivers welfare gains from selection equal to about half a percent per year in the categories covered by our data. Our model features heterogeneous markups because producers of popular products care more about their existing customers while producers of less popular niche products care more about generating new customers. Surprisingly, our model matches the observed trends in household and aggregate concentration without any change in aggregate market power.
The unemployment rate in the United States reached 14.7 percent, with 23.1 million people claiming unemployment benefits, in 2020. While negative effects of unemployment on health and well-being are well understood, the influence of job loss on decision-making has received little attention. Across a controlled experiment (n = 201) and a large-scale survey (n = 32,368), we find that job loss increases risky decision-making. First, we (Sussman and coauthors Daniel O’Leary and Jennifer S. Trueblood) find that an incentive-compatible manipulation of job loss in the lab increases take-up of financial risks. Next, we find evidence of the same relationship in the context of daily life. Job loss among survey respondents is associated with elevated levels of risky decision-making across financial and non-financial contexts. Further, participants who have lost their jobs most recently make the riskiest decisions. These findings have consequential implications for policymakers as the decision to engage in risky behaviors can have negative long-term physical, financial, and psychosocial consequences.
We (Tomy and coauthor Regina Wittenberg-Moerman) study how wholesalers extend trade credit to retailers in economies where formal market institutions, such as financial reporting systems, auditing, and courts, are nonexistent or function poorly. Using the setting of a large market in the northeastern part of India, we find that community membership plays a strong role in the access to trade credit. Wholesalers are more likely to provide trade credit and offer less restrictive credit terms to within-community retailers, are more lenient when these retailers default, and are less likely to experience defaults from them. We show that this cooperation between same-community wholesalers and retailers is achieved through a reciprocity mechanism, which provides insurance against income shocks.